



INTERNATIONAL TAXATION

Second Term, 2002-2003

Instructor: J. Scott Wilkie

MATERIALS

VOLUME I

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**University of Toronto
Faculty of Law**

**International Taxation
Second Term: 2002 / 2003**

J. Scott Wilkie

Course Outline

Course Objective

- To examine the Canadian tax principles and rules that address movements of capital into and out of Canada. “International taxation” may be understood as the system of domestic tax law provisions that apply to transactions, relationships and other arrangements that have an international dimension and, in result, give rise to the possibility of competing tax claims of more than one jurisdiction.
- To examine the manner in which Canada, and other countries, define the portion of their domestic tax base that is attributable to or reflects the influence of economic arrangements in other jurisdictions and, consequently, accommodate the tax claims asserted by other jurisdictions.
- To consider the ways in which Canada’s and other tax systems interact or conflict with each other in light of the principles and tax provisions discussed in connection with the first two objectives.
- To consider contemporary examples of important international tax policy and legislative developments and their influence on actual transactional situations.

Materials and Course Format

- Casebook
- Income Tax Act (Canada)
- Supplemental readings assigned from time to time with respect to particular subjects.
- Instructor notes, which will be distributed throughout the term.

Although the course will be conducted in a traditional lecture format, students will be expected to participate in discussion during the weekly sessions.

Evaluation

- Evaluation will be by way of an examination at the conclusion of the term, during the normal examination period. It will consist of several questions, designed to evaluate students' understanding of the principles of taxation associated with "international tax rules". At least one question will require discussion of the conceptual significance of these rules. The balance will be in a typical problem format. Students will be permitted to use course materials and their notes during the examination; external materials, such as library resources may not be used either directly or in copied form.
- Throughout the term, examples or problems may be assigned for illustrative purposes. They are intended to provide a concrete focus for discussions of the subjects of this course. Students will be expected to have considered these examples or problems in preparation for the course session to which they relate.

Instructor Information

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Meetings about the course can be arranged either at my office or the law school at the student's convenience.

A. INTRODUCTION TO “INTERNATIONAL TAX”

1. OBJECTIVES OF INTERNATIONAL TAX POLICY AND INTRODUCTION TO INTERNATIONAL TAX CONCEPTS

1.1 What Does “International Tax” Mean?

1.2 Basic Concepts and Glossary

1.3 (a) Criteria for Evaluating International Tax Rules

(b) Capital Export Neutrality

(c) National Welfare Neutrality

(d) “Subsidiarity” or National Tax Sovereignty

1.4 Incorporation of Principles in Tax Legislation

1.5 The Multinational Corporation and International Business

2. SIGNIFICANCE OF INTERNATIONAL TAX CONCEPTS

2.1 International Capital Flows

2.2 (a) Jurisdiction to Tax

(b) “Source”

(c) Residence

(d) Nexus

(e) Income Measurement and Attribution

2.3 International Tax Avoidance

2.4 Personal, Corporate Migration

2.5 “Harmful Tax Competition”

2.6 Electronic Commerce

3. CONTEXT FOR “INTERNATIONAL TAX RULES”

3.1 (a) International Investment

(b) Allocation of International Tax Base

(c) Economic Claim

3.2 Reduce “International Tax” Cost

- (a) Location of “Income”/Income Earning Activity
- (b) Avoid Multiple Taxation

3.3 Taxing Residents

- (a) Taxpayer Objectives
- (b) Tax Efficiency

3.4 Taxing Non-residents

- (a) Connection to Jurisdiction

B. THE CANADIAN LEGISLATIVE FRAMEWORK

4. SYSTEMS FOR TAXING RESIDENTS AND NON-RESIDENTS

4.1 (a) *Income Tax Act* (Canada)

- (b) Tax Treaties

4.2 (a) Limits on International Tax Jurisdiction

- (b) International Law
- (c) Constitutional Law

4.3 Income Tax Act: “Parallel Systems”

4.4 System for Taxing Residents

- (a) Business vs. Property Income
 - (a.1) “Active” Business
 - (a.2) “Portfolio” Investment
- (b) “World-wide” Income
- (c) Neutrality Issues

4.5 System for Taxing Non-residents

- (a) Business vs. Property Income
 - (a.1) “Active” Business

(a.2) “Portfolio” Investment

(b) Territorial

(c) Neutrality Issues

4.6 Treaties

(a) Allocate International Tax Base

(b) Mitigate Double Taxation

(c) Mitigate International Tax Avoidance

(d) Resolve International Tax Disputes

5. ASSERTING TAX JURISDICTION

5.1 Source vs. Residence

ITA §§ 2(3), 4, 248(28)

5.2 Personal Jurisdiction

(a) Individuals

(b) Corporations

(c) Other – Trusts, Partnerships

5.3 Residence: Individuals

ITA §§ 250(1)

(a) Measure Connection to Jurisdiction

(b) Distinguish from other connective measures: citizenship, domicile

(c) Basic jurisdictional tests in Income Tax Act and Treaties

(i) OECD Model Tax Convention, Article 4

(ii) Measure Closest Jurisdictional Connection

(d) Legislative tests for Visitors (“Sojourners”) and Certain “Continuing Residents”

(e) “Ordinarily resident”

ITA §§ 250(3)

- (f) Factors
Revenue Canada, IT-221R2
- (g) Part-time Residents
- (h) Overseas Employment Tax Credit
ITA § 122.3
- (i) Dual Residence

5.4 Residence: Corporations

- (a) “Central Management and Control”
- (b) Statutory Rules
ITA §§ 250(4), (5), (5.1) and (6)
- (c)
 - (i) Dual Residence
 - (ii) Corporate Continuation
 - (iii) International Shipping Corporations
- (d) Basic Jurisdictional Tests in Income Tax Act and Treaties
 - (i) OECD Model Tax Convention, Article 4
 - (ii) Measure closest jurisdictional connection

5.5 Residence: Trusts

- (a) General Law
- (b) ITA § 94

5.6 (a) Part Year Residence

ITA § 114

- (b) Changing Residence
 - (i) ITA § 128.1
 - (ii) Short Term Individual Residence
 - (iii) Double Taxation Relief
 - (iv) Special Foreign Tax Credit

- ITA §§ 126(2.21), (2.22)
- Tax Treaty Renegotiations

6. SOURCE OF INCOME

6.1 Meaning and Significance of “Source”, ITA §§ 4

- (a) Geographical source
- (b) Income Quality
- (c) Foreign Tax Credit, ITA §§ 126
- (d) Income Allocation Among Competing Jurisdictions, Treaties

6.2 Periodic Income From Capital

- (a) Interest, Dividends, Rent, Royalties
- (b) Income From the Sale of Property

6.3 Real Property

6.4 Personal Property Not Produced By Taxpayer

6.5 Personal Property Produced By Taxpayer

6.6 Personal Services

6.7 Related To Property Produced/Sold By Taxpayer

6.8 Know-how

6.9 Foreign Exchange

- (a) ITA §§ 39(2); 95(2)(f), (g)
- (b) Revenue Canada IT-95R
- (c) Character and Timing

7. NATURE OF “BUSINESS PRESENCE”

7.1 (a) Electronic Commerce

- (b) Advertising, Invitation to Treat
- (c) Contracts
- (d) Delivery Mechanisms

- (e) Physical Presence in Jurisdiction (Through Third Party Facilities)
- (f) Nature of Property – Typical vs. Digital

7.2 Treaty Rules

7.3 Specific Source Rules

7.4 *Income Tax Conventions Interpretation Act*

C. INTERNATIONAL TRANSACTIONS WITHIN MULTINATIONAL CORPORATE GROUPS

8. SIGNIFICANT TAX ISSUES

8.1 The Multinational Corporation

8.2 International Income Measurement Income Allocation

8.3 (a) Reporting International Transactions

(b) Types of International Transactions

(c) Global Trading

(d) Goods and Services

(e) Intangible Property

8.4 Cost Sharing

8.5 Adjudication of International Income Allocations

8.6 Competent Authority

8.7 APAs (“Advance Pricing Agreements”)

9. TRANSFER PRICING

9.1 International Context

9.2 OECD Model Tax Convention – Article IX

9.3 “Arm’s Length”

9.4 Objectives of Transfer Pricing Rules

(a) ITA § 247 and Revenue Canada Information Circular IC 87-2R

(b) Arm’s Length Terms and Conditions

- (c) Arm's Length Transactions, Transactional Recharacterization
- (d) Documentation
- (e) Penalty
 - (i) Income adjustments
 - (ii) Computation
 - (iii) Relief - Documentation

9.5 Transfer Pricing Analysis

- (a) Typical Methods: "Comparable Uncontrolled Price", Cost Plus, Resale Minus
- (b) Transactional Profit Analysis: Profit Splits and "Comparisons": "Transactional Net Margin Method"
- (c) Cost Sharing
- (d) Methodological Hierarchy
- (e) Entity vs. Branch
- (f) Formulary Apportionment

D. TAXATION OF NON-RESIDENTS: INBOUND INVESTMENT

10. SYSTEM DESIGN

10.1 ITA §§ 2(3), 253; Part XIII

- (a) Direct Income Earning Activities
- (b) Passive Supply of Capital to Residents

10.2 Statutory Framework

- (a) Direct: ITA §§ 2(3), 115, 248(1) ("taxable Canadian property"), 253, 219, 219.1
- (b) Employment
- (c) Carrying on Business
- (d) Disposition of "Taxable Canadian Property"

10.3 Employment

10.4 Business Income

ITA §§ 2(3), 253

(a) (i) “Carrying on”, “in”, “with”

(ii) Relevance of “agency”

(iii) Canadian financial advisors

(b) Branch Tax

ITA § 219

(c) Foreign Bank Canadian Branch, ITA 18(1)(v), 20.2, 142.7, 212(13.3), 218.2

(i) Assimilation to Canadian Subsidiary

(ii) Neutrality issues

(iii) Attribution of Profit

10.5 Thin Capitalization - ITA §§ 18(4) – (6)**10.6 Converting Branch to Subsidiary/Subsidiary to Branch - ITA §§ 219, 219.1 – ITA §§ 69, 85 (special real property rule); 147.2 (Foreign Banks)****10.7 Migration Rules: ITA § 128.1 and § 115****10.8 Distributions**

(a) Return of capital

(b) Dividend

10.9 Non-resident investment corporations

ITA §§ 133

10.10 Tax avoidance: ITA § 245, Treaties**10.11 Taxable Canadian property**

ITA § 115 and 248(1)

(a) Canadian Business Assets

(b) Unlisted Shares of Resident Canadian Corporations

- (c) Unlisted Shares of Foreign Corporations with Substantial Canadian Real Estate Holdings
- (d) Listed Shares of Resident and Non-Resident Corporations
- (e) Rights and Interests, in “TCP”
- (f) Reporting Obligations
 - (i) ITA § 116, 150(1)(a)
 - (ii) Treaty Rules
- (g) Common International Allocation “Conventions”
 - (i) Example: *Canada-United States Income Tax Convention*, Article XIII
 - (ii) Canadian “Departure Tax”, ITA § 128.1

11. NON-RESIDENT WITHHOLDING TAX

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11.1 Management fees

11.2 Interest

11.3 Rent

11.4 Royalties

11.5 Dividends

11.6 Trust income

11.7 Surplus stripping

ITA § 212.1, 212.2

11.8 Non-resident to Non-resident

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11.9 Income attributable to Canadian business presence of non-resident

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11.10 Payment and Administration

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- (a) Direct Income Earning Activity
- (b) “Foreign Direct Investment”

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 - (a.1) Revenue
 - (a.2) Allocating Expenses
- (b) Geographic

- (c) Type of Income
- (d) No Economic Profit
- (e) Short-Term Securities Acquisitions
- (f) Migration

13.2 Non-Business income Tax: ITA §§ 126(1)

- (a) Typically, Withholding Tax
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- (c) Federal, Provincial Tax Credit
- (d) Deduction For Tax Not Creditable/Credited
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- (b) Carryover
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University of Toronto

**International Taxation
Second Term, 2002-2003**

J. Scott Wilkie

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- “Is National Tax Policy Viable in the Face of Global Competition?” by Jack M. Mintz – Special Reports – Tax Notes International July 5, 1999
- “Tax Competition: What (If Anything) To Do About It?” by Hugh J. Ault

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- “Internet Sales Pose International Tax Challenges” by Peter A. Glicklich, Sanford H. Goldberg and Howard J. Levine – Journal of Taxation, June 1996
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- “Canadian Transfer Pricing Rules Keep Pace with International Developments” by J. Scott Wilkie – The Tax Executive March-April 1998
- *Specialty Manufacturing Limited v. The Queen*, 99 DTC
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- “Foreign Tax Credit Planning” by Richard G. Tremblay

- Interpretation Bulletin IT-506 - Foreign Income Taxes as a Deduction from Income
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- “The Foreign Affiliate System in View and Review” by J. Scott Wilkie, Robert Raizenne, Heather I. Kerr and Angelo Nikolakakis
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- “FIEs, NRTs and the World – The Conceptual Framework of the Draft FIE Legislation” by J. Scott Wilkie
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- *Rostland Corporation v. The Queen* [1995] 2 C.T.C.
- *Trans World Oil & Gas Ltd. v. The Queen* [1995] DTC
- Interpretation Bulletin IT-343R – Meaning of the Term Corporation

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- “Are Tax Treaties Necessary?” by John F. Avery Jones
- “Interpretation of Treaties” – Vienna Convention of the Law of Treaties, May 23, 1969
- “Abuse of Tax Treaties” by David A. Ward, Q.C.
- “Interpreting Canada’s Tax Conventions” by James S. Hausman
- *The Queen v. Crown Forest Industries Limited et al* [1995] DTC
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- “A Resident of a Contracting State for Tax Treaty Purposes: A Case Comment on Crown Forest Industries” by David A. Ward, Q.C.
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- “International: A Model Tax Treaty for the Asian-Pacific Region? (Part I)” by Richard J. Vann
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- Excerpts from 2001 OECD Discussion Draft on The Attribution of Profits to Permanent Establishments
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